

In the Supreme Court of the United States

OCTOBER TERM, 1968

No. 776

UTAH PUBLIC SERVICE COMMISSION, APPELLANT

v.

EL PASO NATURAL GAS COMPANY, ET AL.

**ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR
THE DISTRICT OF UTAH**

MOTION FOR MODIFICATION OF OPINION

The United States moves that this Court modify that portion of its opinion in this case dealing with the exchange¹ of a pro rata share of El Paso's outstanding indebtedness for securities of the purchaser of the assets to be divested.

At page 7 of the slip opinion, June 16, 1969, the Court states:

* * * Assumption of \$170,000,000 of El Paso's indebtedness helps keep the two companies in league. The severance of all managerial and all financial connections between El Paso and the

¹ "Assumption" was the term used by the district court (J.S. App. 54) to describe what is in fact an exchange, or "roll-over," of New Company-securities for El Paso bonds and debentures that completely terminates El Paso's liability on its bonds thus exchanged. We use "assumption" herein in the same sense that it was used by the district court.

New Company must be complete for the decree to satisfy our mandate. Only a cash sale will satisfy the rudiments of complete divestiture.

This language would appear to bar the district court from approving any divestiture plan under which a purchaser of the assets now held by El Paso's Northwest Division might reduce the purchase price by assumption of a portion of the relatively low interest obligations now owed by El Paso. Instead, the purchaser would be required to raise a substantial portion of the purchase price by borrowing cash at present high interest rates.² This threatens two undesirable effects. First, it may cause a substantial increase in rates to consumers in the Pacific Northwest presently served by the properties to be divested. Second, it may impair the New Company's ability to compete effectively in California by requiring it to charge correspondingly higher rates to consumers there so as to cover its increased interest costs.

Specifically, therefore, our motion is that the first sentence of the above-quoted language in the opinion be deleted, or, in the alternative, that that sentence be modified so as to permit the district court a measure of discretion with respect to the purchaser's assumption of a portion of El Paso's indebtedness. This mo-

² The Federal Power Commission has held that within limits of safety it is in the public interest for a pipeline to finance major percentages of its investment by debt rather than equity because the tax savings on the interest on the debt will reduce the cost of service and because the return on the equity component of its capitalization necessary to meet governing rate standards will almost always be higher than the cost of debt. See, e.g., *Panhandle Eastern Pipe Line Co.*, 40 FPC 98, 108 (1968).

tion does not question the Court's requirement of a cash sale of El Paso's equity interest in the unlawfully acquired properties.

1. The cost to the New Company of incurring new debt at present interest rates (approximately 8.5 percent) would be at a rate more than 60 percent higher than would have been incurred under the district court's plan permitting assumption as part of the purchase price of a portion of El Paso's indebtedness at an average interest rate of 5.26 percent. Given the Northwest Division's present rates to consumers, the increased debt cost could result, under criteria normally applied by the Federal Power Commission in rate making proceedings, in a rate increase of approximately 9 percent.^{*} Accordingly, the Commission, by a letter to the Solicitor General dated June 27, 1969, and reproduced as Appendix A, *infra*, has expressed "its deep concern" that, unless modified, the opinion "may seriously impair its ability to protect the ratepayers of the New Company * * *."

Nothing in the record indicates that the exchange by the New Company of its debt securities to El

^{*} We assume a return on equity based on recent FPC rulings of 10 percent (see cases collected in *Area Rate Proceedings (Southern Louisiana Area)*, 40 F.P.C. 530, 580); a capitalization for the New Company of 75 percent debt, 25 percent equity; an effective income tax rate passed to consumers of 50 percent; a rate base of \$223,849,000 (El Paso Exh. 57); estimated 1968 revenues to be paid by Northwest Division rate payers at present rates, of \$118,825,000 (El Paso Exh. 1, tab 10); present interest rates, based on recent issues of pipeline debt and the present bank prime rate, of 8½ percent; and an interest rate if the New Company assumes a pro rata share of El Paso's present indebtedness, plus a 1/8th percent additional roll-over cost, of 5.26 percent, as in the district court's plan.

CONTINUED

Paso's creditors for a pro rata share of El Paso's indebtedness will create any community of interest between the two companies that threatens an anticompetitive effect. On the contrary, such an exchange would facilitate the divestiture by offering the purchaser an opportunity to buy the properties at a substantially lower interest cost than presently obtains, thus giving the New Company a cost advantage in calculating rates for competitive service to California, and avoiding the threat of increased rates to consumers in the Northwest.

The plan approved by the district court preserved no financial relationship between El Paso and the

Our calculations further assume that the purchase price will equal or exceed the present rate base value of the property. A reduction below the rate base value sufficient to offset the purchaser's higher interest costs could result, instead, in a burden of higher rates to be borne by consumers served by El Paso. See pp. 7-8, *infra*.

On these assumptions the following calculations can be made:

1. Rate of return:

If debt assumed:

Debt ($75\% \times 5.26\%$)	3.945
Equity ($25\% \times 10\%$)	2.5

Over-all rate	6.445%
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If refinanced:

Debt ($75\% \times 8.5\%$)	6.375
Equity ($25\% \times 10\%$)	2.5

Over-all rate	8.875%
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2. Rate of return applied to rate base:

If debt assumed: ($\$223,849,000 \times 6.445\%$) equals	
\$14,427,068 doubled to cover income taxes	\$28,854,136
If refinanced: ($\$223,849,000 \times 8.875\%$) equals	
\$19,866,598 doubled to cover taxes	\$39,733,197

3. Difference between assumption and refinancing \$10,879,061

4. Effect of difference on revenues at present rates: approximately 9 percent of \$118,825,000 estimated revenues produced by 1968 rates of NW Division \$10,879,061

New Company with respect to the indebtedness to be exchanged. It provided, as part of the purchase price, for the New Company to issue to each El Paso debt holder of New Company, securities in an amount proportional to the Northwest Division's pro rata share of the system-wide debt, at an interest rate equivalent to the rate on the El Paso securities to be assumed, plus an increase of 1/8th of one per cent representing the "roll-over cost" of the exchange. The El Paso creditors were to surrender the El Paso bonds and debentures to be exchanged to El Paso for cancellation. Once the divestiture was accomplished El Paso would have no obligation on the assumed debt, and the New Company would have no obligation to El Paso respecting it. A complete substitution of the New Company for El Paso as the debtor on the obligations exchanged was to be effected.⁴ The creditors involved, representing 99.3 percent of El Paso long term debt holders, are 83 institutional investors including a large number of insurance companies, fraternal organizations, several banks, universities and investment funds, all of which, we are informed, are investors in a wide range of activities.⁵

2. Although it is common for institutional lenders to hold the debt of competing borrowers, the Court may be concerned with the possibility that El Paso-New Company debt holders might attempt to influence the activities of one company to the competitive bene-

⁴ El Paso Exh. 1, p. 11, Tab 17; Implementing Documents, "Agreement," pp. 6, 11-12, 36.

⁵ A complete list of the assenting creditors (El Paso Exh. 1, Tab 15) is set forth in Appendix B, *infra*.

fit or detriment of the other. In view of the number and dispersion of the creditors, this possibility seems remote, but may be an issue which the district court should explore on remand. If it finds, however, that there is no threat that the exchange of the debt will result in anticompetitive influence by the creditors, then we suggest that, in its discretion (and especially in light of any changes that may occur in prevailing interest rates), the district court should be permitted to authorize an assumption of a portion of El Paso's debt by the New Company, provided the terms of such an assumption create no financial relationship between the two firms.

Should the district court find, however, that exchange of the debt is undesirable (because of changed conditions, a threat of anticompetitive consequences or for other reasons), it should then attempt, insofar as feasible, to protect the New Company and its rate payers from the higher purchase costs that ordinarily would result if the debt were not assumed. Since the purpose of the divestiture is to restore competition in the California market to what it was prior to the unlawful merger, any additional burden which results from El Paso's retention of the unlawfully acquired assets during the period of litigation should be imposed on El Paso rather than the New Company. This should be accomplished, however, in a manner which does not simply transfer the burden from rate payers served by the New Company to El Paso rate payers, but which, to the maximum extent possible, imposes

the higher costs of divesting the Northwest Division on El Paso's owners.*

The foregoing paragraph should not, however, be taken as an indication that the district court will necessarily be able to obviate the problem of the purchaser's increased interest costs (in the absence of assumption of a share of the debt) by merely requiring a proportional reduction in the purchase price. In order to assure protection of New Company's rate payers under the criteria normally applied by the Federal Power Commission, such a reduction in the purchase price would have to be sufficient to reduce the cost of the acquired assets on the books of the New Company to a figure which is less than their depreciated original cost (the rate base value of the assets) by an amount equivalent to the effect of the change in the debt costs. This might well require a purchase price which would substantially impair El Paso's equity position, and which might then redound to the detriment of its rate payers. In an effort to protect the latter as well as New Company's rate payers, the district court conceivably might approve an only partially reduced purchase price, subject to a condition that the New Company be required by the Commission to reflect less

* We do not here attempt to describe the form which such protection against additional costs might take. Devising it would undoubtedly require the cooperative efforts of the court in entering the decree of divestiture and the Federal Power Commission in fixing the rates of the resultant companies. Although the Commission has substantial latitude in fashioning its certificate and rate orders, it would, of course, have to act in the context of the purchase price specified by the decree of divestiture. This means that the district court should consider the rate consequences in fashioning its decree, if it decides that assumption of the debt is impermissible.

than its full debt costs for rate making purposes. Such a restriction on New Company's earnings might, however, impede the purpose of the decree by discouraging potential purchasers of New Company as well as reducing the incentive and ability of the purchaser to compete for the California market.

We believe that leaving to the district court discretion to determine whether or not the New Company should be permitted to assume a portion of El Paso's indebtedness as part of the purchase price, and discretion to determine what special protections are necessary if exchange of the debt is impermissible, will enhance the likelihood that a purchaser can be found promptly, and that complete divestiture with a restoration of conditions conducive to competition will be achieved.

Respectfully submitted.

ERWIN N. GRISWOLD,

Solicitor General.

RICHARD W. McLAREN,

Assistant Attorney General.

LAWRENCE G. WALLACE,

Assistant to the Solicitor General.

HOWARD E. SHAPIRO,

Attorney.

JULY 1969.

CERTIFICATE OF COUNSEL

I hereby certify that this motion is presented in good faith and not for delay.

ERWIN N. GRISWOLD,

Solicitor General.

APPENDIX A

FEDERAL POWER COMMISSION,

Washington, June 27, 1969.

Re *Utah Public Service Commission v. El Paso Natural Gas Company*, October Term 1968,
No. 776.

Hon. ERWIN N. GRISWOLD,
Solicitor General
Department of Justice,
Washington, D.C.

MY DEAR MR. SOLICITOR GENERAL:

The Federal Power Commission has asked me to advise you of its deep concern that the Supreme Court's June 16, 1969, opinion in this case may seriously impair its ability to protect the ratepayers of the New Company to whom the El Paso properties will eventually be divested, as well as possibly those of El Paso itself, unless the district court is authorized and directed specifically to take into account the probable rate consequences of its action when such questions reach the Commission.

If, as may well be the case, the Court's opinion is construed to mean that the district court is barred from approving any divestiture plan under which a purchaser of the assets to be divested might assume a portion of the relatively low cost debt obligations now owed by El Paso, it seems clear that the purchaser would have to raise a substantial portion of the purchase price by borrowing at the presently much higher interest rates. Moreover, the alternative of financing all or a substantially larger portion of the acquisition by equity capital would similarly have an adverse

effect upon rates in view of the loss of tax deductions on the interest on the debt and the normally higher cost of equity financing. Accordingly, if the price for the facilities finally ordered to be divested fails to reflect the impact on debt costs of a wholly cash sale, it will be difficult, if not impossible, for the Commission to fail to reflect such costs in its subsequent rate determination for the New Company. For although the Commission has substantial latitude in fashioning its certificate and rate orders, it will have to act in the context of the purchase price specified by the decree of divestiture..

The rates of both El Paso's customers and those of the New Company could also be significantly affected by the reserves reallocation seemingly contemplated by the Court's decision.

In view of the serious nature of these considerations, the Commission strongly urges that they be presented to the Court through an application for rehearing or clarification. In our view such an application should, at the very least, urge that the district court, in fashioning its decree of divestiture, be required to take into account the rate consequences of its actions.

Sincerely yours,

(S) Richard A. Solomon
RICHARD A. SOLOMON,
General Counsel.

APPENDIX B

El Paso Natural Gas Company

**SECURITY HOLDERS INDICATING AGREEMENT IN PRINCIPLE WITH DEBT
SECURITY PROVISIONS SIMILAR TO THOSE IN THIS PLAN OF DIVES-
TITURE**

[Stated in thousands of dollars]

Name (a)	Bonds (b)	Debentures (c)	Total (d)
Aetna Insurance Company.....	\$1,459		\$1,459
Aetna Life Insurance Company.....	25,077	\$14,050	39,126
American National Insurance Company.....	1,105		1,105
Annuity Fund for Congregational Ministers.....		74	74
Bankers Life Insurance Company of Nebraska.....	224	213	437
Board of Lay Trustees, University of Notre Dame Du Lac.....	57		57
The Bowery Savings Bank.....	1,670		1,670
State of California, State Employees' Retirement System.....	13,284		13,284
State of California, State Teachers' Retirement System.....	7,633		7,633
Central Life Assurance Company.....	283	215	498
The Chase Manhattan Bank.....	14,595	522	15,117
Commonwealth Life Insurance Company.....	315		315
Connecticut General Life Insurance Company.....	15,055	4,386	19,441
The Connecticut Mutual Life Insurance Company.....	7,271	2,194	9,465
Continental Assurance Company.....		919	919
Continental Illinois National Bank and Trust Company of Chicago.....	368		368
Country Life Insurance Company.....	170		170
East River Savings Bank.....	1,862	2,991	4,853
The Equitable Life Assurance Society of the United States.....	35,897	33,315	69,212
Equitable Life Insurance Company of Iowa.....	917	919	1,836
Farmers & Mechanics Savings Bank.....	54		54
The Fidelity Mutual Life Insurance Company.....	2,602	147	2,749
The First National Bank of Chicago.....	704		704
The First National Bank, Minneapolis, Minnesota.....	75		75
First National City Bank.....	1,611		1,611
The First Pennsylvania Banking and Trust Company.....		104	104
The Ford Foundation.....	1,800		1,800
The Franklin Life Insurance Company.....	1,330		1,330
Guarantee Mutual Life Company.....	113		113
The Guardian Life Insurance Company of America.....	1,490	2,073	3,563
Gulf Life Insurance Company.....	727		727
John Hancock Mutual Life Insurance Company.....	30,112	13,461	43,573
Home Life Insurance Company.....	2,617	406	2,923
Indianapolis Life Insurance Company.....	283		283
Industrial Indemnity Company.....	98		98
Investors Mutual, Inc.....	6,303	2,609	9,512
Investors Syndicate of America, Inc.....		3,542	3,542
Investors Selective Fund, Inc.....	135		135
Investors Syndicate Life Insurance and Annuity Com- pany.....	270		270
Jefferson Standard Life Insurance Company.....	873	1,365	2,238
The Lincoln National Life Insurance Company.....	3,987	1,946	5,933
The Lutheran Brotherhood.....		675	675
Massachusetts Mutual Life Insurance Company.....	1,963	3,191	5,154
Mellon National Bank and Trust Company.....	2,327		2,327

**SECURITY HOLDERS INDICATING AGREEMENT IN PRINCIPLE WITH DEBT
SECURITY PROVISIONS SIMILAR TO THOSE IN THIS PLAN OF DIVER-
SIFICATION**

(Stated in thousands of dollars)

Name (a)	Bonds (b)	Debentures (c)	Total (d)
Metropolitan Life Insurance Company.....	220,604	48,017	268,711
Modern Woodmen of America.....		854	854
Morgan Guaranty Trust Company of New York.....	2,946	619	3,565
The Mutual Benefit Life Insurance Company.....	6,670		6,670
The Mutual Life Insurance Company of New York.....	20,621	5,843	26,464
Mutual Trust Life Insurance Company.....	142		142
National Life Insurance Company.....	1,737	460	2,197
New England Mutual Life Insurance Company.....	8,610	3,192	11,802
New York Life Insurance Company.....		13,110	13,110
North American Reassurance Company.....	242		242
The Northwestern Mutual Life Insurance Company.....	10,969	3,456	14,427
Pacific Mutual Life Insurance Company.....	2,923		2,923
The Penn Mutual Life Insurance Company.....	1,063	3,324	4,377
The Philadelphia Saving Fund Society.....	3,109	243	3,352
Phoenix Mutual Life Insurance Company.....	2,552		2,552
Pilot Life Insurance Company.....		355	355
Princeton University.....	300		300
Provident Mutual Life Insurance Company of Phila- delphia.....	5,193		5,193
Retirement Fund for Lay Workers of The Congregational Church.....		74	74
The Rockefeller Institute.....	700		700
Royal Neighbors of America.....	425		425
State Farm Life Insurance Company.....	142	181	323
Sun Life Assurance Company of Canada.....	16,727	1,727	18,454
Teachers Insurance and Annuity Association of America.....	1,688	560	2,408
Teachers' Retirement System of Georgia.....		1,320	1,320
The Travelers Insurance Company.....	31,342	6,581	37,923
The Trustees of Columbia University in the City of New York.....	229		229
Trustees of the General Electric Pension Trust.....	8,606		8,606
Union Dime Savings Bank.....	196		196
United Church Board for Homeland Ministries.....		37	37
United Church Board for Homeland Ministries—Ameri- can Missionary Association.....		61	61
United Church Board for Homeland Ministries—Dillard.....		37	37
United Church Foundation, Inc.....		37	37
United States Steel and Carnegie Pension Trust.....	12,819	435	13,254
United States Trust Company of New York.....	449		449
The Volunteer State Life Insurance Company.....		73	73
Wenner-Gren Foundation for Anthropological Research, Incorporated.....	40		40
The Western & Southern Life Insurance Company.....	88		88
State of Wisconsin Investment Board.....	567		567
Total.....	549,197	179,944	729,141

¹Represents 99.2% of the total of \$734,269 of Debt Outstanding.